

HHS FY 1999 FEDERAL MANAGERS FINANCIAL INTEGRITY ACT REPORT ON SYSTEMS AND CONTROLS

A. Background

HHS' management control program under the Federal Managers Financial Integrity Act (FMFIA), reflects the Department's continuing commitment to safeguard the resources entrusted to us by reducing fraud, waste and abuse and preventing financial losses in HHS programs. HHS continually evaluates its program operations and systems utilizing management reviews, systems reviews, CFO financial statement audits and other OIG and GAO audits, etc. to ensure the integrity and efficiency of its operations. Consistent with revised OMB Circular A-123, *Management Accountability and Control* and the *CFO 5 Year Plan*, HHS program managers continue to improve management controls by identifying and correcting management control deficiencies.

The Department's FMFIA program supports a key objective in our CFO 5 Year Plan to respond to our diverse customers' needs by ensuring that the financial information for their programs is accurate and that the financial systems and processes that support them maintain the highest level of integrity.

In addition to our primary goal of obtaining a clean audit opinion on our financial statements, we have a related goal of resolving all internal control material weaknesses and reportable conditions cited by the auditors, as well as those identified through FMFIA management control reviews and systems reviews. OPDIVs need to have written strategies for assessing management controls on an ongoing basis and these strategies for assessing management controls should be consistent with the 1999 CFO 5 Year Plan goals and targets and CFO audit Corrective Action Plans (CAPs).

HHS has developed corrective action plans to address all of the findings resulting from the financial statement audits, including qualifications/ material weaknesses and reportable conditions, and corrective actions are underway. In addition, in response to the May 26, 1998 Presidential Memorandum: "Actions to Improve Financial Management", since July 1998 HHS has reported quarterly to OMB on the status of corrective action for the qualifications in our FY 1998 financial statement audit. We plan to update our corrective action plan in April to reflect the findings from the FY 1999 financial statement audits which are described elsewhere in this Accountability Report.

B. Summary of the Report

The FMFIA Annual assurance required by the Act is contained in the Message from the Secretary at the beginning of this Accountability Report. The details of this year's FMFIA Annual Report, in addition to this narrative summary, are in the statistical summary on page VI - 4.5, which reflects the cumulative total of material weaknesses identified and corrected including a total of six pending material weaknesses. A listing of the six material weaknesses, which includes one new material weakness identified in FY 1999, is shown on page VI - 4.6. The FMFIA-style corrective action plans (CAPs) for the six pending material weaknesses begins on page VI - 4.7.

Three of the six material weaknesses were reported by the auditors in the FY 1999 HHS-wide CFO financial statement audit: 1) Financial Systems and Reporting; 2) Medicare Accounts Receivable; and

3) Medicare EDP Controls. The remaining three material weaknesses are the result of OIG program audits and/or internal management reviews and were included in prior year FMFIA reports.

In last year's report we determined that financial reporting did not reach a level of significance that required reporting to the President and Congress under FMFIA. However, in the FY 1999 HCFA financial statement audits, as well as the audits of several OPDIVs, problems related to account analyses and reconciliation were identified which were deemed material in HCFA under FMFIA. The exhibit, *Financial Systems and Reporting (HHS-99-01)*, contains HCFA's corrective action plan with milestones as well as milestones for addressing the Department-wide financial systems and reporting problems.

Exhibit HHS 99-01 reflects that HCFA did not independently verify the Medicare Hospital Insurance/Supplemental Medical Insurance (HI/SMI) Trust Fund balances, did not reconcile these accounts at a sufficiently detailed level and used ineffective methodologies to calculate HI and SMI transfers. These errors caused the HI Trust Fund to be overfunded by \$14 billion and the SMI Trust Fund to be underfunded by \$18 billion. As a result of these errors, the HI Trust Fund earned excess interest in the amount of about \$154 million and the SMI Trust Fund lost interest earnings in the amount of about \$237 million for FY 1999. HCFA also did not periodically validate the National Claims history file to ensure the existence and completeness of the data. The File was missing 100 million Medicare claims amounting to over \$13 billion – or more than 25 percent of the processed claims – from June until December 1999. HCFA has already developed and begun implementation of a CAP to resolve the trust fund error and prevent a recurrence as reflected in the CAP's milestones which indicate completion in FY 2000. HCFA has also resolved the problem with the National Claims History File.

Regarding Medicare Accounts Receivable (Exhibit HCFA 97-01), HCFA has made substantial efforts to resolve this material weakness which was identified as a qualification by the auditors in the HCFA FY 1997 and FY 1998 financial statement audits. The short-term milestones to address the FY 1998 audit qualification have been implemented and the qualification has been reported as resolved in the FY 1999 financial statement audit. However, the long-term solution to the Medicare accounts receivable issue is the development of an integrated accounting system for Medicare contractors which is planned for FY 2004.

This report also reflects the combining of two 1998 material weaknesses for Medicare EDP into one. This is consistent with the FY 1999 HHS-wide and HCFA CFO financial statement audits, which identify Medicare EDP as one material weakness with two parts. The two parts of the Medicare EDP material weakness are reflected in this report as follows: (a) *Improve Medicare Contractors Systems Application Controls, Exhibit HCFA 98-01a* (formerly HCFA 98-01); and (b) *System Access Controls at HCFA Central Office, Exhibit HCFA 98-01b* (formerly HCFA 98-02). The CAPs for these material weaknesses reflect that corrective action is now scheduled for completion in FY 2000.

C. CFO Financial Statement Audits and the FMFIA

In the FY 1998 CFO financial statement audits, certain OPDIVs were cited by the auditors for a reportable condition based on the fact that their 1998 FMFIA Reports did not report an FMFIA material weakness for each of the CFO audit material weakness. We have been working closely with OIG staff on an approach to bring the 1999 FMFIA Report and the CFO audits closer together as follows:

- All material weaknesses and instances of systems non-compliance with the Federal Financial Management Improvement Act (FFMIA) identified in the FY 1998 CFO audits, including any which the OPDIV may be aware of from the 1999 CFO audit at the time they prepared their FMFIA Report, were required to be reported to the Department. This is also consistent with Revised OMB Circular A-123 that requires that "...a deficiency should be reported if it is or should be of interest to the next level of management."
- OPDIVs were asked to recommend which, if any, of their CFO audit material weaknesses and FFMIA non-compliances should be included as an FMFIA material weakness in the Department's Report, i.e., are significant enough to be reported outside the agency to the President and Congress.
- Under existing departmental policy a corrective action plan is required for all CFO audit material weaknesses which are tracked under the CFO audit process. However, for those material weaknesses and FFMIA non-compliances the OPDIV recommends for inclusion in the Department's FMFIA Report, OPDIVs were required to include a corrective action plan in the FMFIA format and submit it with their report. Those material weaknesses which resulted from the CFO audits and are included in the Department's 1999 FMFIA report were described under "Section B" above.

However, all of the audit material weaknesses, with the exception of those discussed in Section B, are not included in the Department's FMFIA report because HHS believes that the remaining material weaknesses do not reach a level of significance that require reporting to the President and Congress as defined under Revised OMB Circular A-123. Further, as stated previously, HHS requires corrective action plans to address all of the findings resulting from the CFO financial statement audits, including qualifications/ material weaknesses and reportable conditions. Reporting all CFO audit material weakness in the Department's FMFIA report would duplicate the CFO process.

D. Federal Financial Management Improvement Act (FFMIA) and Section 4 FMFIA

The auditor's opinion on the Department-wide FY 1999 CFO financial statement audit identified three instances of non-compliance with the FFMIA, which are reported elsewhere in the HHS Accountability Report. The FFMIA non-compliances are as follows:

1. The accounting systems used by HHS and the operating divisions were not adequate to prepare reliable and timely financial statements (also known as financial systems and reporting).
2. HCFA did not have an integrated accounting system to capture expenditures at the Medicare contractor level.
3. The HCFA central office and Medicare contractor access and application control weaknesses were significant departures from requirements of OMB Circulars A-127, Financial Management Systems, and A-130, Management of Federal Information Resources.

(1) Financial Systems and Reporting

As stated above, HHS is declaring a Departmentwide material weakness in financial systems and reporting in this year's Report. The auditors reported instances of non-compliance including: adjusting financial statement amounts but not the underlying general ledger; using accounts not prescribed by the U.S. Standard General Ledger (SGL); and not posting accounts in accordance with prescribed SGL rules. However, HHS systems remain in overall compliance with Section 4 of the FMFIA.

(2) Financial Management Controls at the Medicare Contractors

Regarding financial management controls for Medicare contractors, HCFA has made substantial progress; however its efforts to complete corrective action, including efforts to implement an integrated accounting system for HCFA and the Medicare contractors, have been delayed due to the need to first address Y2K issues. HCFA has now developed a long range multi year plan for an integrated general ledger system. In the meantime, HCFA continues to utilize information collected from the contractors for the standard general ledger as part of the entry into HCFA's accounting system, which is validated through reviews performed by central office staff. Therefore, the Department believes that the lack of an integrated accounting system at this time does not constitute an FMFIA Section 4 non-compliance.

(3) EDP Controls

As reported above, HCFA has carried over two material weaknesses from the FY 1998 report addressing the need for EDP controls including systems access and application controls at the HCFA central office and the Medicare contractors. Full resolution of these issues was delayed because of Y2K initiatives. The OIG acknowledged in its findings that HCFA had made substantial improvement in the areas of systems access control, application software development and change control. HCFA has developed a Corrective Action Plan to resolve this finding in FY 2000.

The Payroll EDP processing systems control issues cited in FY 1998 were resolved.